(5)

No. 91-194

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

QUILL CORPORATION,

Petitioner,

v.

STATE OF NORTH DAKOTA,
BY AND THROUGH ITS TAX COMMISSIONER,
HEIDI HEITKAMP,

Respondent.

On Writ of Certiorari to the Supreme Court of the State of North Dakota

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BRIEF FOR THE STATES OF NEW HAMPSHIRE, DELAWARE AND MAINE AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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INTERESTS OF *AMICI CURIAE*

The States of New Hampshire, Delaware, and Maine file this brief as *amici curiae* in support of Petitioner Quill Corporation. The States urge reversal of the decision below, which rejects *National Bellas Hess, Inc.* v. *Department of Revenue*, 386 U.S. 753 (1967), as "obsolescent precedent," and holds, in defiance of *Bellas Hess*, that consistent with the Commerce Clause a State can require an out-of-state business to act as that State's use-tax collection agent when it has no physical presence in that State.

Amici have an interest in protecting their State economies from the parochial tax revenue policies of North Dakota and other tax-aggressive States. *Amici* urge this Court to adhere to its historical practice under the Commerce Clause of entrusting to Congress complex questions of national economic policy such as those that would be involved in a decision to replace the bright-line "physical presence" test of *Bellas Hess* with an amorphous "economic presence" rule.

Amici believe that the short-term revenue gains some individual State and local tax authorities might reap from overturning *Bellas Hess* would be far outweighed by the long-term adverse consequences for the economies of the Nation and of the *amici* States. Such a decision, because of the cumulative burdens it would place upon vendors who do business by mail, would, among other things, restrict the ability of consumers to obtain ready access to products that are available only by mail or in large cities, lead to a rise in consumer prices, threaten the viability of small and emerging enterprises that continue to be one of the few sectors of the economy to create new jobs, and encourage just the sort of balkanization of trade among the States that the Commerce Clause was intended to prevent.

SUMMARY OF ARGUMENT

I. This Court has long held unconstitutional any State requirement that a mail-order business with no physical presence in the State collect use taxes on sales to residents of that State. *National Bellas Hess, Inc.* v. *Department of Revenue*, 386 U.S. 753 (1967). There is no basis for the opinion of the North Dakota Supreme Court below that the bright-line rule of *Bellas Hess* is "obsolescent" or for overruling *Bellas Hess*. Anything less than a reaffirmance of the "physical presence" test would encourage costly and widespread litigation.

North Dakota's argument here appears to be driven by a parochial desire to maximize that State's revenue at the

expense of national economic values that are the foundation of the Commerce Clause. If that argument is accepted, interstate mail-order businesses—most of them small and moderate-sized enterprises—could be required to calculate and remit taxes to as many as 6,500 governmental entities with as many as 90 different sales and use tax rates and widely varying definitions of taxable items. While computer technology has advanced since 1967, the number and complexity of such taxes have also increased dramatically, and there is no evidence that the practical considerations underlying *Bellas Hess* have disappeared.

II. Whether the bright-line rule of *Bellas Hess* should be changed, and if so to what extent and in what manner, is a question that is properly reserved for the exercise of Congress's power to regulate interstate commerce. Congress continues to consider the question, and is uniquely positioned to fashion any alternative to the "physical presence" test and to tailor any change in the law to the exigencies of smaller businesses.

III. A. Even if the Court were to examine anew the Commerce Clause question raised by the North Dakota statute, the Court should reach the same conclusion it reached in 1967 in *Bellas Hess*. This Court has consistently recognized that allowing one State or local jurisdiction to require use tax collections by out-of-state vendors who receive no substantial State services would invite the thousands of other taxing authorities to do likewise, and that the resulting cumulative burdens upon interstate commerce must be considered under the Commerce Clause.

B. The cumulative burdens upon companies that sell by mail are as significant today as they were when *Bellas Hess* was decided. North Dakota's proposal to substitute an amorphous "economic presence" rule for this bright-line test would require out-of-state mail-order sellers to master and to keep abreast of the volumes of ever-changing rates, exemptions, and classifications set forth in State and local use-tax schemes; to supplement and

continuously update advertisements and catalogs in order to inform consumers of the details of possibly applicable taxes; to cooperate with costly and time-consuming tax audits; to incur substantial added expenses in the recordation of sales and inventory; and either to prepare to litigate the fact-specific question of "economic presence" in gray-area cases throughout the country, or to overcollect and overpay use taxes in order to avoid the time and expense of such litigation. The cumulative effects of such regulation would be to suppress interstate commerce in ways that inevitably would lead to higher prices and to depriving consumers, especially those in relatively isolated areas, of ready access to a full range of products.

C. Effective alternative means—such as Maine's use-tax statute—already exist by which individual States that wish to collect use taxes on their residents' out-of-state purchases can do so without unjustifiably burdening out-of-state vendors.

IV. If the Court were to overrule *Bellas Hess*—as it should not—the Court should state expressly that such a decision would apply only prospectively. Retroactive application of a new "economic presence" rule would result in staggering financial liability for interstate businesses that reasonably relied on *Bellas Hess*. Silence on this subject could, under *James B. Beam Distilling Co.* v. *Georgia*, 111 S. Ct. 2439 (1991), lead to the imposition of just such retroactive liability; at a minimum, it would lead to prolonged uncertainty and widespread, costly litigation.

ARGUMENT

I. OVERRULING *BELLAS HESS* WOULD SACRIFICE THE CERTAINTY OF THE BRIGHT-LINE RULE UPON WHICH A SUBSTANTIAL ELEMENT OF THE NATIONAL ECONOMY IS FOUNDED, MERELY TO SERVE THE SHORT-TERM PAROCHIAL REVENUE INTERESTS OF SOME STATES

In more than a half century of decisions weighing the constitutionality of State laws requiring out-of-state vendors to collect State use taxes, this Court has enforced a "sharp distinction" between out-of-state mail-order sellers who maintain "retail outlets, solicitors, or property within a State," and "those who do no more than communicate with customers in the State by mail or common carrier as part of a general interstate business." *National Bellas Hess, Inc.* v. *Department of Revenue*, 386 U.S. 753, 758 (1967).[1] These decisions allow a State to compel only those vendors who maintain a physical presence in the State, and thereby substantially benefit from State services, to collect and remit use taxes for the State's benefit. *See id.* at 756-60.[2]

In *Bellas Hess*, the State of Illinois requested this Court "to obliterate" this basic distinction. *Id.* at 758. The State urged the Court to adopt instead an amorphous "economic presence" rule, under which Illinois could have required out-of-state vendors maintaining no physical presence in Illinois to serve as State tax collectors. *See id.*; *Bellas Hess* Brief for Appellee at 33-34. The Court

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[1] *See also National Geographic Soc'y* v. *California Board of Equalization*, 430 U.S. 551 (1977); *Miller Bros. Co.* v. *Maryland*, 347 U.S. 340 (1954); *Nelson* v. *Montgomery Ward & Co.*, 312 U.S. 373 (1941); *Nelson* v. *Sears, Roebuck & Co.*, 312 U.S. 359 (1941).

[2] For purposes of convenience, we follow the practice of the court below (and commentators) of referring to the "sharp distinction" in *Bellas Hess* as the "physical presence" test. *See, e.g., State by Heitkamp* v. *Quill Corp.*, 470 N.W.2d 203, 207, 211-12 (N.D. 1991).

refused to do so. The Court found it difficult to conceive of commercial transactions more exclusively interstate in character than mail-order transactions, and observed that such purely out-of-state mail-order businesses do not receive the same substantial State services that in-state businesses receive. The Court further noted the intolerable burdens that would be visited upon out-of-state mail-order sellers if other States and the then-existing 2,300 local taxing authorities were allowed to impose similar tax-collection obligations upon them, entangling them "in a virtual welter of complicated obligations to local jurisdictions." 386 U.S. at 758-60 & n. 12. In so holding, the Court reaffirmed that

> [t]he very purpose of the Commerce Clause was to ensure a national economy free from such unjustifiable local entanglements. Under the Constitution, this is a domain where Congress alone has the power of regulation and control.

Id. at 760.

Today, North Dakota requests this Court to approve a statute that in all material respects is identical to the one this Court struck down in *Bellas Hess*. The North Dakota Supreme Court would have this Court reject *Bellas Hess* as obsolescent. *State by Heitkamp* v. *Quill Corp.*, 470 N.W.2d 203, 208 (N.D. 1991). Although the court below also contends—erroneously, as we shall show in Part III of this brief—that the legal principles underlying *Bellas Hess* have changed, that is plainly not the driving force behind North Dakota's position. Rather, the reason North Dakota seeks to reinterpret the Constitution, as well as the foundation for its argument here, is that the volume of mail-order sales has grown greatly in recent years. It is this which the North Dakota court characterizes as "the greatest change" since *Bellas Hess*. 470 N.W.2d at 209. This increase in sales volume has motivated North Dakota to argue, and its Supreme Court to agree, that interstate mail-order vendors have been

flourishing and that financially pressed State and local governments should therefore be allowed to tax their sales, even though they receive none of the benefits of State services that in-state retailers receive.

Amici are well aware of the need of State and local governments to increase tax revenues. Rhetoric about mail-order businesses seeking a "tax-free mail order haven" or a tax-free "niche," *id.* at 214-15, however, is no substitute for hard analysis as to whether North Dakota's taxation scheme is unconstitutionally burdensome, or whether other, less disruptive means of collecting use taxes exist, or, indeed, whether a costly system of uncoordinated, multijurisdictional use-tax collection, which would invite retaliatory "trade wars,"[3] is within the legislative prerogative of individual States rather than Congress.

The fact that many interstate mail-order businesses have succeeded financially in the years since *Bellas Hess* is reason to applaud that opinion, not to criticize it. *Bellas Hess* is anchored in the bedrock Commerce Clause belief that such an unrestrained circulation of commodities among the States would, as has in fact happened, open up and replenish "veins of commerce" in every State. *See* Hamilton, *The Federalist No. 11*.[4] Pejorative

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[3] Such a system would disproportionately benefit some States and disadvantage others. For example, four large State governments (California, New York, Texas, and Illinois) would receive approximately one-third of the additional tax revenues collected. Robert R. Nathan Associates, Inc., "An Economic Study of the Likely Impact of Overturning the *Bellas Hess* Decision on State Tax Revenues" 4 (1986). States that have a large proportion of mail-order sellers and/or that have no State use tax would be adversely affected, thus inviting retaliation. Prevention of such "trade wars" among the States is a major purpose of the Commerce Clause. *See generally Sporhase* v. *Nebraska ex rel. Douglas*, 458 U.S. 941 (1982); *A&P Tea Co.* v. *Cottrell*, 424 U.S. 366 (1976).

[4] *See also H.P. Hood & Sons, Inc.* v. *DuMond*, 336 U.S. 525, 539 (1949); Collins, *Economic Union As A Constitutional Value*, 63 N.Y.U.L. Rev. 43, 45 (1988).

terms such as "tax haven" and "tax-free niche" envince a fundamental disregard for what this Court has repeatedly extolled as the Commerce Clause's "guarantee of a free trade area among States." *American Trucking Ass'ns* v. *Scheiner*, 483 U.S. 266, 281 (1987); *see also id.* at 280, 283, 284; *Boston Stock Exchange* v. *State Tax Comm'n*, 429 U.S. 318, 328 (1977).[5]

Furthermore, North Dakota's statute is not restricted to regulating the large success-stories of the mail-order business.[6] It reaches struggling and marginally successful firms as well as prosperous ones. It burdens new and emerging out-of-state vendors just as it hampers old and established ones. It conscripts small New Hampshire arts-and-crafts enterprises, Maine lobster cooperatives, and Delaware non-profit museums as well as large, multistate conglomerates. The only distinction North Dakota law makes—and it is hardly a distinction at all—is between those out-of-state vendors that transmit three or more mailings into the State over the course of any twelve-month period and those that send two or fewer.[7] Thus, North Dakota regulates every mail-order business—large or small—that makes the most minimal effort to reach North Dakota residents.

The reasoning of the opinion below depends upon the court's general assertion that *Bellas Hess* has been rendered obsolete by changes in technology since 1967. 470

[5] In this respect, as in others, the Framers were centuries ahead of their time: North Dakota asks this Court to authorize the erection of balkanizing trade barriers among the States at that precise moment in history when European nations are rushing to tear down such barriers as a means of reinvigorating their individual state economies. *See* "Making Europe a Mighty Market," N.Y. Times, May 22, 1988, at C1.

[6] In this important respect it differs from recent legislative proposals before Congress, to which we refer in the next Part of this brief. *See* H.R. 2230, 101st Cong., 1st Sess. (1989); S. 480, 101st Cong., 1st Sess. (1989).

[7] *See* 470 N.W.2d at 205 (citing N.D. Admin. Code § 81-04.1-01-03.1(3)).

N.W.2d at 215. Given the centrality of this contention, it is startling that the lower court opinion limits its discussion on the point to the *ipse dixit* that automated accounting systems and advancements in computer technology have greatly alleviated the burdens of collection. *Id.*[8] In fact, however, the cumulative burdens on interstate mail-order businesses would still be considerable today, particularly in view of the growth in the number of taxing entities and the complexity of their use-tax schemes. Indeed, the burdens would be even greater today for small and emerging businesses than they were in 1967.

The number of taxing jurisdictions has dramatically increased since 1967. At the time of *Bellas Hess*, approximately 2,300 jurisdictions were empowered to impose sales and use taxes. 386 U.S. at 759 & n.12.[9] Today, if State and local taxing authorities were permitted to follow North Dakota's lead, a mail-order vendor with sales in all fifty States could be required to comply with the use-tax regulations of approximately 6,500 State and

[8] The court does offer a "see" citation to three legal publications, but none of them justifies the court's conclusions. For example, the author of two of the three sources, Paul J. Hartman, not only advocates Congress's assuming an active role in this area, but also concludes that if this Court were to overturn *Bellas Hess* and there were no such congressional action, "compliance cost burdens associated with collecting and remitting the use tax in multiple jurisdictions would remain a serious problem, especially for the smaller out-of-state sellers." Hartman, *Collection of the Use Tax on Out-of-State Mail-Order Sales*, 39 Vand. L. Rev. 993, 1015 (1986). The other commentator relied upon by the court below, McCray, *Overturning Bellas Hess: Due Process Considerations*, 1985 B.Y.U.L. Rev. 265, 290 (1985), merely mentions in passing that computers ease administrative burdens, and then explicitly states that the cumulative-burdens issue is outside the scope of the article.

[9] Although data are not always available on use taxes *per se*, the Court pointed out that in most States local sales taxes are complemented by use taxes. *Id.* at n.12 (citing H.R. Rep. No. 565, 89th Cong., 1st Sess. 872 (1965)).

local jurisdictions.[10] In 1967, only eight different rates of sales and use taxes existed. *Id.* at 759 n.13. Today, States impose ninety different sales and use tax rates.[11] Statutes and regulations setting forth technical product classifications and detailed exemptions also abound.[12]

To be sure, there have been great advances in computer technology since 1967. As we explain below, however, these advances only go so far, and would be of least assistance to vendors who would be most imperiled financially by an overruling of *Bellas Hess*. Moreover, they cannot compensate for the additional cumulative costs that all out-of-state mail-order vendors would incur in advertising and printing; in lost or more complicated sales transactions; in fulfillment of post-transaction payment, reporting, and audit obligations; and indeed in obtaining counsel as to what taxes are due and to whom they should be paid. These are cumulative regulatory burdens that the various jurisdictions' tax laws do not impose on local businesses; imposing the burdens on mail-order vendors therefore would discriminate severely against them.

While times have changed, they have not changed so much so that the craftsmen, apparel manufacturers, developers of specialty items, booksellers, and thousands of other entrepreneurs who advertise their products by mail, many of whom cannot compete with big-company brands for retail shelf space, should be saddled with burdens that this Court for fifty years has held to be unconstitutional under the Commerce Clause. Nor have times changed so

[10] *See* Advisory Commission On Intergovernmental Relations, *State And Local Taxation Of Out-Of-State Mail Order Sales* 6 (1986).

[11] *See* [1991] 1A All-State Sales Tax Rep. (CCH) ¶¶ 19-005 to 19-056. Some of these rates extend into four and five digits— *e.g.*, 4.725, 5.9375, 6.0625, and 6.513 percent. *Id.* at ¶¶ 19-030, 19-036, 19-053.

[12] *See id.* at ¶¶ 8-305 *et seq.*

much that the Court should be indifferent to the economic effects of overruling *Bellas Hess*: some vendors would inevitably reduce the number of States in which they do business, while others would go out of the mail-order business altogether; jobs would be lost; access to certain products would be restricted; and, as a result of decreased competition among sellers, the price of many products would ineluctably rise.[13]

II. IF THERE IS TO BE ANY CHANGE IN THE BRIGHT-LINE RULE LIMITING USE-TAX COLLECTION TO ENTERPRISES HAVING A PHYSICAL PRESENCE IN THE TAXING STATE, CONGRESS MUST MAKE THAT CHANGE

This Court has recognized that if the Commerce Clause means anything, it is that fifty States cannot effectively regulate the complexities of interstate commerce. *See Bellas Hess*, 386 U.S. at 760.[14] When the Court deferred to Congress in *Bellas Hess*, it noted that Congress had shown an active interest in the area of state use-tax regulation of interstate businesses. *Id.* at 760 n.15. In recent years, Congress has again shown interest,[15] but has yet to be persuaded that *Bellas Hess* should be overturned. This Court should not authorize aggressive taxing States to do that which Congress so far has refused to allow.[16]

[13] *See generally* Mittelstaedt & Stassen, *The Macromarketing Effects of the Taxation of Interstate Mail-order Sales*, 11 J. Macromktg. 46, 53-55 (1991).

[14] *Accord H.P. Hood & Sons, Inc.* v. *DuMond*, 336 U.S. 525, 534 (1949) ("The necessity of centralized regulation of commerce among the states was so obvious and so fully recognized that the few words of the Commerce Clause were little illuminated by debate").

[15] *See supra* note 6.

[16] In the analogous area of State taxation of income derived from interstate commerce, Congress has acted and has rejected an "economic presence" test. *See* 15 U.S.C. § 381 (States cannot tax

Article I, Section 8 makes clear that the intricacies of interstate commerce are properly the subject of legislative, not judicial, regulation.[17] No one can seriously dispute the need to exempt modest-sized out-of-state businesses from the burdens of complying with the regulations of thousands of use-tax schemes. Yet precisely how such an exemption should be crafted is uniquely a legislative task. A judicially created, case-by-case "economic presence" test—borrowing, as it does, from this Court's highly fact-specific "minimum contacts" due process jurisprudence—is no answer: it is too amorphous, invites too much (and too expensive) litigation, and diverts attention from the fundamental economic issues with which the Commerce Clause is concerned, such as the cumulative effects of a State regulation upon interstate commerce. Only Congress could substitute a workable "economic presence" rule for the bright-line "physical presence" test of *Bellas Hess*. *See, e.g.*, S. 480, 101st Cong., 1st Sess., § 2 (1989) (permitting States to require use-tax collection by interstate businesses whose total annual U.S. sales exceed $12.5 million or whose sales in the taxing State exceed $500,000). Similarly, Congress alone is qualified to propose a comprehensive solution to the problem of disuniformity among State and local use-tax schemes. *See id.* at § 3 (requiring uniform rates among all of the local jurisdictions within a State as a prerequisite to those jurisdictions' being able to reach out-of-state businesses).

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income derived from the solicitation of orders which are sent outside the State for approval and which are to be filled by delivery from out-of-state vendors). Indeed, Congress believed that limits on State authority were necessary to address the "burdens of compliance" on out-of-state companies. S. Rep. No. 658, 86th Cong., 1st Sess. (1959), 1959 U.S. Code Cong. & Adm. News 2548, 2549-50.

[17] Article I, § 8, gives Congress the authority to "regulate Commerce * * * among the several States." The Court's practice of deferring to Congress in this area has made review of congressional action under the Commerce Clause largely a formality. L. Tribe, *American Constitutional Law* § 5-8 (2d ed. 1988).

III. NORTH DAKOTA'S TAXING SCHEME IMPOSES UNCONSTITUTIONAL COLLECTION, REPORTING, AND PAYMENT OBLIGATIONS ON OUT-OF-STATE MAIL-ORDER BUSINESSES

The above discussion explains why the Court should continue to resolve cases such as this under the "physical presence" standard rather than under a vague economic rule that would encourage litigation in a myriad of individual cases. Even if the Court were to examine anew the constitutional question raised by the North Dakota statute—as it need not do—the Court should reach the same conclusion it reached in 1967 in *Bellas Hess*. That is, any State use-tax collection statute would be inconsistent with the Commerce Clause if applied to vendors having no physical presence in the taxing State. Thus, the Court should reaffirm the "physical presence" test. Failure to do so would be to authorize a full-blown economic analysis every time a State develops a novel theory by which to regulate out-of-state businesses. The result would be years of costly and widespread litigation.

A. The Commerce Clause Prohibits State And Local Regulatory Requirements Whose Cumulative Effects Unjustifiably Burden Interstate Commerce

Bellas Hess rests upon the core proposition that some State taxes or regulations, even if not obviously discriminatory in themselves, would create cumulative burdens on interstate commerce that are unacceptable under the Commerce Clause if adopted by enough States (or local jurisdictions). The Court concluded in *Bellas Hess* that, whether or not the burdens placed upon interstate mail-order businesses by Illinois' use-tax scheme, standing alone, were impermissibly high, the cumulative burdens that would have been created if other States and local taxing authorities had been allowed to enact similar schemes would have been unjustifiable. "[I]f Illinois can impose such burdens," the Court reasoned, "so can every

other State, and so, indeed, can every municipality, every school district, and every other political subdivision throughout the Nation with power to impose sales and use taxes." 386 U.S. at 759.

Given the variations in State and local tax rates, allowable exemptions, and administrative and recordkeeping requirements, the Court concluded in *Bellas Hess* that allowing State and local taxing authorities to compel out-of-state mail-order businesses with no physical presence in their respective jurisdictions to collect, record, and remit use taxes pursuant to their different use-tax schemes, would have unconstitutionally entangled those vendors in a web of complicated obligations to local jurisdictions. *Id.* at 759-60.

Weighing the cumulative burdens on interstate commerce in order to determine the constitutionality of a given practice conforms with longstanding Commerce Clause jurisprudence. *See, e.g., Nippert* v. *City of Richmond*, 327 U.S. 416, 430, 431 (1946); *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. 250, 255 (1938). It has recently been employed by this Court to invalidate State economic regulation and tax schemes. *See Healy* v. *Beer Institute, Inc.*, 491 U.S. 324, 336 (1989) (evaluation of a statute under the Commerce Clause must include inquiry into "what effect would arise if not one, but many or every, State adopted similar legislation"); *American Trucking Ass'ns* v. *Scheiner*, 483 U.S. 266, 285 & n.20 (1987).

In *Nippert*, for example, the Court struck down a city ordinance imposing a license fee on local and non-local solicitors alike because of the cumulative burdens such a practice, if adopted elsewhere, would place upon interstate businesses:

> [T]he cumulative effect, practically speaking, of flat municipal taxes laid in succession upon the itinerant merchant as he passes from town to town is obviously greater than that of any tax of statewide application

> likely to be laid by the legislature itself. And it is almost as obvious that the cumulative burden will be felt more strongly by the out-of-state itinerant than by the one who confines his movement within the State or the salesman who operates within a single community or only a few.

327 U.S. at 429-30.

Similarly, this Court examined the cumulative effects of a Pennsylvania tax statute in *Scheiner*. That statute imposed facially neutral flat taxes equally upon in-state and out-of-state trucks traveling Pennsylvania highways, although Pennsylvania trucks on average traveled five times as many miles on Pennsylvania highways as did out-of-state trucks. "In practical effect," the Court reasoned, the taxes "impose a cost per mile on [out-of-state] trucks that is approximately five times as heavy as the cost per mile borne by local trucks * * *." 483 U.S. at 286.[18] The Court emphasized that if every State enacted similar legislation, there would be "no conceivable doubt that commerce among the States would be deterred." *Id.* at 284-85 & nn.16, 20 (citing *Nippert* with approval). The Court consequently concluded that Pennsylvania's flat-tax statute was discriminatory, posed "manifold threats to the national free trade area," and therefore violated the Commerce Clause. *Id.* at 285-86.

This Court's Commerce Clause decisions also make clear that the cumulative costs of compliance with different State and local regulations can make an otherwise constitutional statute unconstitutional. The compliance costs in *Bellas Hess* related to an out-of-state seller's keeping itself abreast of the variations in State and local tax rates and allowable exemptions, and to additional administrative needs and recordkeeping obligations. 386

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[18] *See also* 483 U.S. at 296 ("imposition of the flat taxes for a privilege that is several times more valuable to a local business than to its out-of-state competitors is unquestionably discriminatory and thus offends the Commerce Clause").

U.S. at 759-60. The principle that such compliance costs can lead to a statute's invalidation under the Commerce Clause also long predates *Bellas Hess*. *See Southern Pacific Co.* v. *Arizona*, 325 U.S. 761, 773-74 (1945).

Given this solid doctrinal foundation upon which *Bellas Hess* rests, the North Dakota Supreme Court had no basis for dismissing it as obsolete. The court's attempt to demonstrate that "the legal landscape" has changed since *Bellas Hess*, 470 N.W.2d at 209-13, is altogether unconvincing. For example, the court suggests that *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977), undermines *Bellas Hess*. *See* 470 N.W.2d at 209-11. It does not. Unlike Petitioner, Complete Auto was physically present in the taxing State and did not even contend that there was an insufficient nexus with the taxing State. 430 U.S. at 277-78.[19] Moreover, the present case concerns a State's regulatory authority to require out-of-state businesses to collect and remit State taxes levied upon others,

[19] There is no disputing the fact that, like Bellas Hess, out-of-state mail-order vendors such as Petitioner do not utilize such State and local services as fire and police protection, transportation facilities, or public roads. The North Dakota court placed considerable weight on the notion that North Dakota provides trash collection services that indirectly benefit mail-order sellers insofar as the State or local government disposes of catalogs mailed to North Dakota residents. 470 N.W.2d at 218-19. There are at least three major problems with the court's transforming this notion into a conclusion that North Dakota's statute is, for this reason, constitutional. First, it proves too much: *every* interstate business that utilizes the postal service transmits material requiring disposal in the destination State. Second, such an attenuated connection to the taxing State is fundamentally different from a business's taking direct advantage of State services. It may be that the mailings impose some costs on the State where the recipients live, but that does not constitute a service or benefit to the *mailer*. Third, as we discuss in the text, this sort of "minimal contacts" due process analysis is inappropriate for Commerce Clause purposes because it unduly distracts attention from the central economic questions with which the Commerce Clause is concerned—the actual impact on interstate commerce of a given State regulatory requirement.

not, as in *Complete Auto*, a State's authority to require an out-of-state business to pay a tax itself.

The most fundamental error in the North Dakota court's reliance on *Complete Auto*, however, is that the four-part test articulated there is fully consistent with *Bellas Hess*. *Complete Auto* held that a tax will pass muster under the Commerce Clause *only* if the tax: (1) is applied to an activity that has a substantial nexus with the taxing State, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the State. *Id.* at 279; *see also D.H. Holmes Co.* v. *McNamara*, 486 U.S. 24, 31 (1988). This Court has subsequently made clear—*e.g.*, in *Commonwealth Edison Co.* v. *Montana*, 453 U.S. 609, 625-26 (1981)—that *Bellas Hess* is the touchstone of the first prong ("substantial nexus") of the *Complete Auto* test. Here, as in *Bellas Hess*, there is no sufficient nexus to support a tax-collection requirement, without even reaching the burdens that are relevant to other prongs of the *Complete Auto* test.

North Dakota's tax scheme fails at least two other prongs of the *Complete Auto* test. As we demonstrate below, the scheme imposes discriminatory burdens in its operation against out-of-state businesses, and the tax-collection obligations it creates are not "fairly related to the services provided by the State." [20]

[20] The other cases the North Dakota court offered as evidence of an altered legal landscape also do not support its conclusion. In each case the out-of-state business maintained a physical presence in the taxing State. For example, D.H. Holmes Co. was properly required to pay a Louisiana use tax on catalogs delivered into Louisiana from out-of-state printers because D.H. Holmes was a Louisiana corporation, owned and operated thirteen stores in Louisiana, and employed approximately 5,000 workers in the State. *See D.H. Holmes Co.* v. *McNamara*, 486 U.S. at 26, 32. Similarly, the out-of-state manufacturer in *Tyler Pipe Indus., Inc.* v. *Washington State Dep't of Revenue*, 483 U.S. 232, 250-51 (1987), maintained

B. The Substitution Of An "Economic Presence" Rule For The "Physical Presence" Test Of *Bellas Hess* Would Create Unconstitutional Cumulative Burdens On Interstate Commerce

1. *Increased advertising and printing costs*

Mail-order businesses incur substantial costs in publishing and mailing catalogs and in purchasing advertising space in newspapers, magazines, and other publications. The more advertising space the companies need in order to explain tax information to consumers, the greater these costs. One of the consequences of overruling *Bellas Hess* would be to force out-of-state mail-order companies to purchase considerable additional advertising space so as to provide purchasers with necessary use-tax information.

If every State and local taxing authority adopted a use-tax provision like that of North Dakota, a mail-order business selling its goods nationally would be required to list and explain all potentially applicable tax rates, classifications, and exemptions, as well as to identify separately those States that apply their tax rates to shipping and handling charges and those States that do not.[21] Explanation of exemptions, which are often of dizzying complexity, would be particularly cumbersome. As this Court

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active sales representatives in the taxing State, and the companies in *National Geographic Soc'y* v. *California Board of Equalization*, 430 U.S. 551 (1977), and *Standard Pressed Steel Co.* v. *Washington Dep't of Revenue*, 419 U.S. 560 (1975), operated offices or had employees in the taxing States.

[21] *See Interstate Sales Tax Collection Act of 1987 and the Equity in Interstate Competition Act of 1987: Hearings on H.R. 1242, H.R. 1891, and H.R. 3521 Before the Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary*, 100th Cong., 2d Sess. 207, 234 (1988) ("*1988 Hearings*") (statement and testimony of William T. End, then-Executive Vice-President of L.L. Bean, Inc.).

pointed out in *Bellas Hess*, 386 U.S. at 759-60 & n.14, determining which items are exempt under a particular State's law is often unclear, and may be beyond the capacity of any mechanical system.[22] Pennsylvania, for example, does not tax "clothing," but does tax clothing "accessories," "formal day or evening apparel," and "sporting goods and clothing not normally used or worn when not engaged in sports."[23] Some States tax certain kinds of food, but not others.[24] California, which aggressively enforces its complex use-tax laws, has recently amended them to tax "snack foods" while exempting "food products"; "Ritz crackers are deemed taxable, but saltine crackers are not."[25] Taxing jurisdictions also frequently grant exemptions on the basis of a purchaser's identity; thus, out-of-state vendors must track which charitable organizations each jurisdiction exempts. *See, e.g.*, 72 Pa. Stat. Ann. § 7204(10).

Printing single-state or regional catalogs would not solve the problem because it costs more to print numerous regional or single-state catalogs and because, in order fully to inform consumers, those catalogs would still have

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[22] More recently, some witnesses before Congress have testified that computer tax programs are not able to recognize tax exemptions for products, which vary by jurisdiction, or judge whether products fit within a given exemption. *See, e.g., Interstate Sales Tax Collection Act of 1987: Hearing on H.R. 1242 Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways and Means*, 100th Cong., 1st Sess. 178 (1987) (testimony of Heath Kline); *Collection of State Sales and Use Taxes by Out-of-State Vendors: Hearing on S. 639 and S. 1099 Before the Subcomm. on Taxation and Debt Management of the Senate Comm. on Finance*, 100th Cong., 1st Sess. 53 (1987).

[23] 72 Pa. Stat. Ann. § 7204(26).

[24] *See, e.g.*, N.D. Century Code § 57-40.2-04.1 (1991 Supp.).

[25] "Sales Tax Nightmare on Main Street," Forbes, Sept. 30, 1991, at 37; *see* Cal. Rev. & Tax Code § 6359, as amended by ch. 88, S.B. No. 179.

to contain complete nationwide tax information. This is so because most States require mail-order vendors to collect the use tax of the jurisdiction to which goods are sent. Thus, when a purchaser instructs the vendor to deliver the goods to another person—which often occurs in the case of gifts—the purchaser must be told how to calculate the use tax of every possible destination jurisdiction.[26] This is a significant problem, among other reasons, because mail-order businesses derive between sixty and seventy-five percent of their total revenues during the holiday gift season.[27]

2. *Diminished sales, increased collection costs, and increased payments to cover taxes unremitted by customers*

Ideally, a mail-order customer reads the advertisement or catalog to determine the size of the payment he or she should remit, calculates the amount of any applicable tax, and pays the total amount due.[28] As the complexities of determining the applicable tax rate and the scope of possible exemptions increase, however, so does the burden on the consumer in accurately calculating the tax amount and the resulting total price. The result is an increase in

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[26] [I]f I order three presents from Talbot's and have it sent to a brother in New Jersey, a brother in Texas, and a sister in Wisconsin, I have to calculate a separate tax rate for each of those items, I have to look under each State's exemptions to determine whether clothing is exempted or is not in that State, I have to check each State to know whether or not the postage handling charge is or is not exempted from the State. I then have to make all of those calculations and run a total.

1988 Hearings at 234 (testimony of William T. End).

[27] *See* "The War of the Christmas Catalogues," N.Y. Times, Nov. 15, 1991, at D1.

[28] *See* Note, *Collecting the Use Tax on Mail-Order Sales*, 79 Geo. L.J. 535, 540 (1991).

lost sales as potential purchasers become discouraged,[29] and—as more and more purchasers underpay or fail to pay any tax—increased collection costs[30] and increased payments to the taxing State by the vendor out of its own pocket to cover deficiencies.[31]

These problems are somewhat mitigated when the mail-order customer pays by credit card, because then the customer can furnish the mail-order vendor with an account number and rely upon the vendor to calculate correctly all applicable use taxes. But this flexibility in credit-card sales is of limited value because nearly fifty percent of mail-order customers pay by check.[32] And any such open-ended payment arrangement is bound to result in customer resistance, inquiries, and disputes. Also, the additional cost of collecting unpaid taxes is particularly burdensome for a mail-order vendor with inexpensive products or few orders.[33] *See* Note, *Collecting the Use Tax on Mail-Order Sales*, 79 Geo. L.J. 535, 540 (1991).

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[29] *See 1988 Hearings* at 206 ("The success of direct marketing depends upon making the transaction as simple as possible. Once we make mail order complex and confusing for our customers, we discourage their doing business with us.") (statement of Willliam T. End).

[30] *1988 Hearings* at 89 (testimony of Direct Marketing Association). Some direct marketers experience an approximately nine-percent underpayment by customers of the total taxes due. *Id.*

[31] Since statutes such as North Dakota's hold the mail-order vendor liable whether or not the State resident encloses the proper use-tax sum, the mail-order vendor faces the following choices when there is mispayment or nonpayment by the consumer in a check transaction: return the order to the customer and request full payment (thereby endangering the sale), fill the order and request the customer to remit the tax in a second check, or pay the tax for the customer.

[32] *1988 Hearings* at 86 (testimony of Direct Marketing Association).

[33] A study by a national accounting firm concludes that the single most significant variable affecting collection costs is size of the

3. *Increased administrative and audit costs*

Just as out-of-state mail-order companies would be required to remit taxes, directly or indirectly, to as many as 6,500 different jurisdictions, so too would they have to comply with a host of uncoordinated recordkeeping and record-production requirements of those jurisdictions. Computers could help generate records, but companies still would have to purchase the necessary computer software and the annual software renewal, and would have to hire personnel to input data, operate the computers, and remit the taxes. Even small companies would be subject to time-intensive, business-disrupting audits by a myriad of different taxing jurisdictions.

4. *Increased expenses to determine where taxes are due*

Under the bright-line "physical presence" test of *Bellas Hess*, a mail-order company has a fairly clear idea of when it is subjecting itself to a jurisdiction's requirement to collect use taxes. By contrast, under an amorphous "economic presence" rule, a vendor would have to retain counsel to educate itself as to the probabilities of whether —under a particular State's statutory scheme and federal case law—the company's contacts with customers in that State are sufficient for the State to hold the company liable for the collection of use taxes. A vendor would also have to decide whether to incur the costs of overpaying or to risk incurring litigation expenses and possible penalties. Such expenses are obviously particularly burdensome for smaller vendors.

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company. The larger the company, the smaller the cost of collection (generally) as a percentage of total sales or of taxes collected. *1988 Hearings* at 87 (testimony of Direct Marketing Association).

C. North Dakota Has Available To It A Less Burdensome Alternative Means For Collecting Use Taxes From Mail-Order Customers

Even in the absence of congressional action, States such as North Dakota have alternative constitutional ways of taxing the use of products shipped in-state by out-of-state mail-order vendors. Maine, for example, requires its residents to calculate use-tax liability when completing their annual tax returns, which include a specific line-item for a use-tax declaration.[34] Taxpayers who do not know the exact amount they owe, or cannot be bothered to calculate it, are permitted simply to multiply their adjusted gross income by .0004 [35] and report the resulting figure as their use-tax liability. The State makes the computation and automatically adds the tax to the taxpayer's total tax liability if the taxpayer fails to compute the tax. The success Maine has had in collecting use taxes illustrates that other collection mechanisms are available to States. The virtue of Maine's system, of course, is that it does not impermissibly burden interstate commerce. North Dakota's system, on the other hand, does, and it should be declared unconstitutional for the reasons articulated by this Court in *Bellas Hess*.

IV. ALTERNATIVELY, IF THE COURT WERE TO OVERRULE *BELLAS HESS* AND ADOPT A NEW RULE, THE COURT SHOULD EXPRESSLY STATE THAT THE NEW RULE WOULD HAVE ONLY PROSPECTIVE EFFECT

If this Court were to adopt a new rule (*e.g.*, an "economic presence" rule) and not expressly make it non-

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[34] *See* Me. Rev. Stat. Ann. tit. 36, § 1861-A. Line 14 on Maine's 1040 short form and line 19 on the long form require taxpayers to calculate and to declare any outstanding use tax liability for the preceding year.

[35] The tax rate of .0004 is based upon the application of the Maine sales tax rate to the national yearly average of mail-order purchases.

retroactive, the Court's recent decision in *James B. Beam Distilling Co.* v. *Georgia*, 111 S. Ct. 2439 (1991), suggests that lower courts would have to apply that new rule retroactively in other similar cases. This could result in crushing back-tax and tax-penalty liability for mail-order vendors in the *amici* States who had a right to rely on *Bellas Hess* and the "physical presence" test. *See generally Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971). One State has already notified out-of-state vendors of its intention to issue assessments for past liability in the event this Court were to overrule *Bellas Hess*.[36]

Amici therefore would urge the Court, in the event the Court were to depart from a "physical presence" standard, to make explicit, in accordance with its usual practice when overruling clear past precedent, *see Chevron Oil*, 404 U.S. at 106, that mail-order companies with no physical presence in a taxing State would not be subject to liability for use taxes and penalties related to sales made prior to the date of this Court's decision.[37] This would, *inter alia*, avoid prolonged uncertainty and vexatious and costly litigation by States seeking to enhance their revenues.

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[36] Notice, dated November 15, 1991, from William D. Marshall, Acting Administrator, Sales and Use Tax Division, Ohio Department of Taxation (noting that few court decisions are only prospective, and announcing the Department's intention to issue assessments on sales made over many years if this Court affirms the lower court's decision).

[37] Although the Court did not grant certiorari on the retroactivity question presented by Petitioner, we understand *James B. Beam Distilling Co.* to hold that the issue of retroactivity as a choice of law is implicit in every case.

CONCLUSION

For the foregoing reasons, *amici* respectfully request this Court to reverse the judgment below. Alternatively, *amici* request that any affirmance of the decision below make clear that mail-order vendors having no physical presence in a taxing State may not be held liable for use taxes and penalties related to sales made prior to the date of this Court's decision.

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